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**BEFORE THE  
DEPARTMENT OF TRANSPORTATION  
WASHINGTON, D.C.**

Computer Reservations System (CRS) Regulations	) ) ) )	Docket Nos. OST-97-2881 OST-97-3014 OST-98-4775
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**REPLY COMMENTS OF GALILEO INTERNATIONAL, L.L.C.**

Galileo International, L.L.C. ("Galileo") hereby submits its reply comments in connection with the Department's Supplemental Advance Notice of Proposed Rulemaking concerning computer reservations systems ("CRSs"), 65 Fed. Reg. 45551 (July 24, 2000) ("Supplemental Advance Notice").

**INTRODUCTION**

The comments the Department has received cover a wide range of issues, including some that go beyond the scope requested by the Supplemental Advance Notice.<sup>1</sup> We address here some of the broad issues that emerge from the initial round of comments, then turn to some specific points that warrant further comment.

Galileo continues to believe that most CRS regulation should be eliminated as unnecessary, and that the emerging Internet channel should not be subjected to onerous CRS-style regulation. Because the industry has learned to live with the CRS rules, however, Galileo does not object to a continuation of those rules,

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<sup>1</sup> Galileo has addressed many of these points in its prior comments in this proceeding.

although some clarification and amendment may be needed to assure that all CRSs have an equal opportunity to compete. And, in view of the fast pace of change in both the CRS business and travel distribution practices generally, Galileo urges the Department to provide for an early sunset date for any CRS regulations.

The comments the Department has received – from carriers, CRS vendors, traditional travel agents, Internet travel service providers, and other interested parties – present quite different, sometimes starkly different, pictures of airline travel distribution issues, and advocate different, sometimes inconsistent, rules. A number of commenters seize the opportunity to suggest rules crafted to advantage their own interests relative to their suppliers, their distributors, and/or their competitors. Thus, for example, Expedia advocates regulation of its major CRS competitors and many of its on-line competitors, but not of Expedia itself, while Orbitz would draw the line in a manner to ensure that it remains free from the regulations it advocates for CRSs. We trust that the Department will see these kinds of self-interested proposals for what they are, and that it will not allow its regulatory power to become a tool that serves one interest unfairly at the expense of others.

One notable feature of the comments, taken as a group, is that they often attempt to justify expansive proposals for new regulation with no more than generalized assertions about potential harms, or supposed benefits. They offer very little in the way of specific data to back up these assertions; the commenters simply ask the Department to accept them as givens. But those who advocate regulation, especially expansive new regulation, bear a burden to show just why such regulation

is required. And the Department likewise has an obligation to support any regulation it adopts with a sound basis in policy and the factual record.

The Department's guiding policy for regulation should be twofold: First, it should regulate only when a compelling case has been made to justify regulation.<sup>2</sup> Second, the Department must regulate evenhandedly, so that whatever burdens it may impose fall equally on all competitors, and all competitors have the same opportunity to compete in all channels of distribution. It is fundamentally unfair to impose special regulations on Galileo that its competitors would not face. Moreover, regulations that burden some competitors and not others will distort competition, impede innovation, and allow less-efficient companies to thrive at the expense of others that are more efficient and productive. The Department must regulate all to the same extent or regulate none.

## DISCUSSION

The discussion below addresses first the rules governing CRSs and then the subject of Internet services.<sup>3</sup>

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<sup>2</sup> The Department has previously made clear that CRS regulations will be imposed only to prevent substantial reductions of competition among airlines, or to protect consumers from misleading information, and that no regulation will be adopted unless the public benefits substantially outweigh the costs. See 65 Fed. Reg. 45551, 45556 (July 24, 2000); 62 Fed. Reg. 47606, 47607-09 (Sept. 10, 1997); 57 Fed. Reg. 43780, 43781 (Sept. 22, 1992).

<sup>3</sup> In view of the wide range of arguments advanced in the initial comments, Galileo has not attempted to respond to every point. Instead, this reply covers only those subjects that appear to be of greater significance.

## **I. CRS REGULATION**

### **A. Competition in the CRS Business**

A number of the initial comments, but particularly those of Orbitz, argue broadly that CRS regulation must continue because competition is lacking in the CRS business. While Galileo does not object to continuation of the existing CRS rules (so long as these rules are applied evenhandedly), we note that the assertions about lack of competition in the CRS business are wholly inconsistent with Galileo's experience.

As Galileo has explained in earlier comments in this and other proceedings, far from enjoying a "cozy environment" (Orbitz Comments at 11), Galileo and other CRSs are under relentless pressure to invest heavily in improving their services in order to stay competitive.<sup>4</sup> CRSs constantly innovate to provide ever higher levels of functionality for participating carriers and subscribers. As just one example, CRSs have worked hard in the last few years to develop electronic ticketing capability for numerous airlines.<sup>5</sup> Moreover, CRSs must scramble every day in the marketplace to retain business and win new subscribers. All four CRSs offer significant financial incentives to obtain and keep subscribers. It is common for travel

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<sup>4</sup> The suggestion by American Airlines, Midwest Express, and others that CRSs are "essential" (e.g., American Airlines Comments at 28, Midwest Express Comments at 3-6) apparently is intended to recall the "essential facility" doctrine that was invoked as a justification for the original CRS regulations. But any argument that a CRS constitutes an "essential facility" is plainly incorrect in view of the many channels of distribution that are available today. CRSs provide a very valuable, cost-effective means for carriers to distribute their services, and carriers have found that, on balance, the benefits of participating in each CRS exceed the costs. But that favorable cost-benefit evaluation does not make a CRS (or even all CRSs collectively) an "essential facility."

<sup>5</sup> See pages 2-3 of Galileo's September 22 comments for a description of some of the innovative CRS services Galileo has developed in the past few years.

agents to ask Galileo to renegotiate a subscriber contract to provide better terms after the agent is approached by one or more other CRSs seeking to convert its business. With the advent of more travel distribution options, including new on-line services, CRSs must work even harder to retain business.

Moreover, CRSs have brought numerous competitive benefits to the air transportation business. As a result of extensive investments in the development of CRSs over the past 25 years, the airline industry enjoys an unparalleled distribution system. CRSs have played an important role in making possible an enormous expansion in the volume of air travel, allowing airlines to sell far more efficiently than they could otherwise. Thanks to CRSs, new entrants can instantly gain valuable exposure to travel agents worldwide, creating opportunities to attract passengers. The high speed and huge transaction capacity of CRSs allow airlines to offer fare sales and schedule changes as market conditions change day to day. The efforts of CRSs in turn have stimulated the entry of new Internet competitors, providing wider distribution choices for the traveling public.

The vigorous competition among CRS vendors and the competitive benefits CRS services provide for air transportation, along with the diminished role of airlines in ownership and management of CRSs and entry of new on-line competitors, suggest that there is little need for regulation of CRSs themselves. As described in our initial comments, to the extent abuses remain, they tend to involve airline practices rather than CRS conduct. In particular, airlines have in some instances declined to participate fully in some CRSs or have attempted to tie airline benefits to usage of a particular CRS. Thus, to the extent the Department concludes that there is

a continuing need for regulation, it would make more sense to impose selected rules on airlines, rather than on CRSs.<sup>6</sup> In any event, there is plainly no basis for increased regulation of CRSs.

**B. Mandatory Participation Rule**

Several commenters argue that the Department's mandatory participation rule, 14 C.F.R. § 255.7, should be eliminated. Others take the position that the rule should be retained and that it should be expanded to cover marketers of CRSs.

If the Department concludes that CRS regulation should continue, the mandatory participation rule must continue as well. The problem addressed by the rule is not merely a hypothetical one. In the past, some airline owners of other CRSs have declined to participate in the Apollo® system at the same level as they participated in their own systems, apparently with the intent of enhancing the appeal of the owner's CRS.<sup>7</sup> The lack of full participation by such an owner prevents a CRS from competing effectively because it makes that CRS less attractive in relation to the owner's CRS, particularly in cities where the owner has a large percentage of the

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<sup>6</sup> To the extent the Department has doubts about its authority to regulate those CRSs that have no airline ownership, imposing regulation directly on airlines, rather than on CRSs, would help ensure even-handed regulation.

Some commenters argue that all CRSs can be regulated regardless of airline ownership or other affiliation because CRSs are within the statutory definition of "ticket agent". The statutory language does not support this argument. See 49 U.S.C. § 40102(a)(40). A CRS merely provides information and the facility through which others (the airline and its agent) may sell or arrange for transportation. In this regard, a CRS is little different from an Internet service provider that supplies a medium through which information regarding travel is exchanged and purchases are made.

<sup>7</sup> See page 7 note 10 below for one significant example.



lift.<sup>8</sup> The mandatory participation rule promotes CRS competition because it allows all CRSs to offer a high level of functionality, which in turn benefits travel agents and their customers and corporate accounts. The rule also promotes competition in air transportation by ensuring that travelers have access to all airlines' services on a roughly equivalent basis, without arbitrary limitations.

Northwest's argument that mandatory participation should extend only to a "basic" level of participation should be rejected.<sup>9</sup> A carrier's provision of a premium level of functionality in its own CRS, while offering only the "basic" level in a competing system, can impede the ability of the competing system to win subscribers. Moreover, participation at the "basic" level deprives CRS users of useful information and functionality. Northwest's own past conduct illustrates the need for a strong rule on this subject.<sup>10</sup>

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<sup>8</sup> Such conduct has effects similar to the tying of airline benefits to use of a particular CRS. Galileo argued in its opening comments (at pages 11-12 & note 11) that the Department should clarify or amend its rules to ensure that they prohibit certain airlines' practices of tying discounted fares for corporate accounts to usage of a particular CRS.

<sup>9</sup> See Comments of Northwest Airlines, Inc. at 5-7.

<sup>10</sup> Northwest has repeatedly attempted to provide a lower level of functionality in the Apollo® system than in Northwest's own CRS. Galileo's predecessor, Covia Partnership, initially brought this problem to the Department's attention in 1991. See Opening Comments of Covia Partnership in Response to Notice of Proposed Rulemaking, June 24, 1991, at 53-54 & Tabs A & F (describing the refusal of Northwest Airlines to participate fully in the Apollo Inside Link® feature and attaching sales literature promoting Northwest's CRS on the basis that automatic last seat availability for Northwest flights was available only through that CRS). Subsequently, Northwest continued to discriminate against the Apollo® system, and Covia eventually pursued an informal complaint against Northwest with the Department. Northwest finally upgraded its participation level in Apollo®, but only after a lengthy delay.

In order to ensure that all CRSs have an equal opportunity to compete, the mandatory participation rule should be extended to those airlines that market a CRS. The Department has already defined CRSs to include systems that are marketed by airlines and has permitted contract restrictions to be imposed on marketers as well as owners of CRSs.<sup>11</sup> The Department should promptly expand the coverage of the mandatory participation rule in a similar manner to ensure that all CRSs have the necessary information and functionality to provide them with an equal opportunity to compete.

As some commenters suggest, it ultimately may be appropriate to extend the mandatory participation rule to airlines that have other types of commercial relationships with CRSs. At present, however, it is at least clear that airlines that market a CRS should have an obligation to participate in other systems to the same extent as CRS owners.

### **C. Marketing Data**

The current rules require that a CRS make available to all U.S. participating carriers (and to non-U.S. participating carriers under certain circumstances) all marketing, booking, and sales data relating to carriers that it generates from its system. 14 C.F.R. § 255.10. Several commenters urge that the Department eliminate this rule or even ban the release of marketing data without the

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<sup>11</sup> See 14 C.F.R. § 255.2; 62 Fed. Reg. 59797 (1997) (discussing “parity clauses”). Extension of the mandatory participation rule and other “system owner” requirements to system marketers would be consistent with the recent amendment to the International Air Transportation Fair Competitive Practices Act, 49 U.S.C. § 41310(g), which authorizes action against marketers of non-U.S. CRSs, as well as owners of such systems.

consent of a carrier or travel agent, while retaining other CRS regulation.<sup>12</sup> There is no basis for such arguments.

The original purpose of the requirement that marketing data be made available to all participating carriers was to enhance airline competition by preventing CRS owner airlines from obtaining an unfair advantage over non-owner airlines.<sup>13</sup> CRS vendors have complied with the requirement by making available aggregated data for sale to all eligible carriers.<sup>14</sup> Galileo is aware of no complaints that CRS owners have obtained preferential access to marketing data in recent years.

Galileo believes that sale of CRS marketing data has had procompetitive results, permitting carriers to gain a better understanding of the markets they serve and those in which they may wish to initiate service. The Supplemental Comments of Delta Airlines, dated September 25, 2000, confirm that carriers use CRS data to increase the efficiency of their operations. For example, Delta notes that it uses such data to assist it in route planning (particularly international route planning, where other sources of information are scarce) and to respond to market changes. As Delta states, “[b]y enabling carriers to respond quickly to changes in market demand, CRS data helps airlines to optimize service patterns, discount (sales) programs and other incentives offered to consumers and travel agents.” Delta Suppl. Comments at 31.

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<sup>12</sup> See, e.g., Comments of the Air Carrier Association of America; Comments of America West at 15.

<sup>13</sup> See 49 Fed. Reg. 11643, 11666-67 (1984).

<sup>14</sup> Marketing data sold by CRSs do not include passenger names or other identifying information about individual travelers. Thus, sale of such data does not raise concerns about protection of individual privacy.

Critics of the Department's marketing data rule insist that only large carriers benefit from CRS data because such data are too expensive for new entrants and other small carriers to purchase. Whether or not this was the case in the past, the situation is different now. Within the past few years, all CRS vendors have begun to offer smaller packages of data, thereby allowing small carriers to purchase only information of particular relevance to their operations. For example, with Galileo's Selective MIDT product, introduced in 1998, each month a carrier can choose to receive regional data sorted by, among other things:

- Country, U.S. state or Canadian province of the subscriber
- Region of the subscriber (Europe, Middle East, Africa, North America, South America, Asia, Australasia)
- Country pairs, based on journey to/from (origin and destination)
- Regional pairs, based on journey to/from (origin and destination)

A carrier can obtain a limited set of Galileo MIDT data for as little as \$5,000 per month. Galileo also offers MIDT Impact™, a service that allows a carrier to obtain analyses of marketing data tailored to its own needs.

With these options, smaller carriers can target their purchases and analyses of marketing data to gain maximum benefits at minimum cost. There is no reason small carriers cannot obtain the same sorts of efficiency and competitive benefits from marketing data as large carriers like Delta. For example, a new entrant carrier could use CRS data to help determine which routes are good candidates for entry.

Galileo's experience confirms that it is not just large carriers that find marketing data to be useful. More than 45 airlines, including a number of smaller carriers, subscribe to Galileo MIDT services.

Several commenters argue that large carriers use CRS marketing data as part of an effort to drive smaller carriers out of their hubs or routes. However, these commenters offer no evidence to support their claims. The comments do not include even one example of a situation in which a larger carrier allegedly has used CRS data in an effort to drive out or otherwise disadvantage a smaller carrier, much less a situation in which such an effort allegedly has succeeded.

Other commenters complain that access to marketing data gives the airlines a commercial advantage in their dealings with travel agencies and corporations. But, in view of the many procompetitive uses of marketing data, the solution to any such problem should be to disseminate the information more widely, not to cut it off. Galileo is prepared to offer marketing data to any subscriber, so that airlines would no longer have special access to the information.<sup>15</sup>

It is worth noting that there are international implications associated with restrictions on release of marketing data. A number of years ago, European Union officials strongly protested the inability of European carriers to obtain U.S. CRS data, while U.S. carriers were free to obtain data generated by European CRSs.<sup>16</sup> The

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<sup>15</sup> To the extent any party can show that a carrier or travel agent recipient of marketing data has used the data in an inappropriate way, the Department could take action against the recipient pursuant to its Section 411 authority. Alternatively, the antitrust laws provide enforcement tools that can be used to remedy anticompetitive uses of marketing data.

<sup>16</sup> Docket No. 49745, et al., Exemption for U.S. Computer Reservations Systems

Department ultimately granted exemptions from its restrictions, so that non-U.S. carriers would be able to obtain data generated by U.S. CRSs so long as the non-U.S. systems affiliated with those carriers were subject to comparable obligations.<sup>17</sup> A new move to shut down access to U.S. CRS data could provoke another dispute. Ultimately, U.S. carriers could be disadvantaged relative to European carriers as a result of such a dispute.

Any suggestion that CRSs are not entitled to sell marketing data is off the mark. The output a CRS sells to customers originates with a proprietary database compiled through the extensive efforts of the CRS. CRSs invest substantial resources to create these databases. In creating a database, the CRS takes input from many different sources, combines it, systematically arranges it, and stores it pursuant to a defined structure. The CRS formats the data on tapes, cartridges, or other electronic media and licenses its use to customers.

Galileo's fundamental concern about marketing data is at bottom a commercial concern: Marketing data present a revenue opportunity. In response to a governmental mandate, CRSs invested resources to develop the capability of processing and selling such data. Over the years, Galileo and other CRSs came to view data sales as a commercial opportunity and worked to develop that opportunity.<sup>18</sup> As described above, Galileo now offers a number of different products,

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under 49 U.S.C. 40109 from section 255.10(b) of the CRS rules, Final Order, served Oct. 24, 1994, at 3.

<sup>17</sup> *Id.* at 9-10.

<sup>18</sup> The revenue Galileo earns from the sale of marketing data helps to cover Galileo capital investment and operating costs. This in turn allows Galileo to keep booking fees and subscriber charges lower than they otherwise would be.

tailored to the differing needs of its customers. In order to enhance its capabilities in this area, Galileo in 1998 acquired Shepherd Systems, a market leader in the design and implementation of advanced travel industry sales and marketing information systems.

It would be entirely inappropriate for the Department, having mandated the sale of marketing data and watched as CRSs invested in developing that line of business, now to undercut the business through further regulation. Galileo and other CRSs made significant investments in the expectation that they would be able to continue sale of marketing data. As a matter of fundamental fairness and economic sense, the Department should not take steps that would “strand” these investments in development of the MIDT market without a compelling justification. Because the comments fail to provide any evidence that would support a prohibition on the sale of CRS data, the Department should reject such proposals.

#### **D. CRS Booking Fees**

Very few commenters seek specific action on the subject of fees charged by CRSs. However, a small number argue that the Department should impose various limitations on the structure of booking fees, while at least one commenter argues for full-fledged regulation of the level of CRS fees.<sup>19</sup>

The arguments for CRS fee regulation are misguided. The Department currently requires that fees charged to participating carriers be nondiscriminatory, and CRSs have structured their fees to be consistent with that limitation. But there is no basis for further restrictions. Galileo addressed booking fee issues at length in its

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<sup>19</sup> See, e.g., Comments of Midwest Express Airlines at 21-22.

1997 and 1998 comments in this proceeding, and we refer the Department to those comments.<sup>20</sup> Here we merely summarize some of the more significant points.

As an initial matter, contrary to the assertions of some commenters, CRS fees are not unreasonably high. CRSs provide extremely valuable services to carriers, allowing them to save millions of dollars in promotional and reservations staff costs. At the same time, CRSs must spend hundreds of millions of dollars each year to maintain the huge infrastructure that makes possible the reliable processing of thousands of transactions per second, day in and day out. CRSs must earn revenues sufficient to cover these huge investments.

CRS booking fees are not out of line with processing fees charged for far simpler transactions in other industries. Fees for standard Apollo® services range from 32 cents for a cancellation to \$1.40 for input of an active confirmed segment.<sup>21</sup> Addition of extra functionality (e.g., both Interactive Sell™ and Inside Availability®) could push a segment fee up to \$1.80. But even if a reservation includes several

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<sup>20</sup> See Comments of Galileo International, L.L.C. in Response to Advance Notice of Proposed Rulemaking, filed Dec. 11, 1997, at 26-40; Reply Comments of Galileo International, L.L.C., filed Feb. 3, 1998, at 9-16.

<sup>21</sup> Galileo charges \$1.90 for input of a ticketed passive segment in Apollo®. Galileo formerly imposed a lower charge for all types of passive segments. However, many airlines complained that they should not be charged for passive bookings that do not involve issuance of a ticket, and travel agents' generation of passive bookings resulted in numerous disputes between carriers and travel agents. In 1998, Galileo responded to these concerns by adopting a policy of charging fees in the United States only for those passive bookings that involve issuance of a ticket.

No charge is assessed for many other Apollo® transactions, such as provision of availability displays, building of connections, quotation of fares, and cancellation of a ticketed passive segment.



segments and is rebooked several times using the maximum level of functionality, the total fees are likely to be only a tiny fraction of the ticket price.

In comparison, Telecharge and Ticketmaster charges are in the range of \$5 to \$10 per transaction.<sup>22</sup> Thus, for a \$40 ticket, the purchaser could pay processing fees of as much as 25 percent of the face value of the ticket.<sup>23</sup>

No commenter has shown that CRSs are earning monopoly profits. And none has even attempted to propose a workable scheme of CRS fee regulation.<sup>24</sup> The Department should reject any arguments for regulation of the level of CRS fees as lacking in support.

Proposals to limit the types of transactions for which CRSs charge fees are also without merit. Some airlines suggest that CRSs be permitted to charge only for transactions that involve actual travel. But CRSs are not in the airline business;

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<sup>22</sup> See "Strings Attached; Add-On Charges, Handling Fees Leave Some Concert-Goers Hearing Sour Notes," *The Plain Dealer*, July 17, 2000, p. 1E (Ticketmaster "convenience" fees average \$5 to \$7 per ticket for processing, plus \$3 in "handling" fees for each order; convenience fee may be as high as \$11); "How to Get Tickets," *The Washington Post*, Apr. 16, 2000, p. E10 (Telecharge adds a service charge of \$5.75 per ticket for Broadway shows, \$4.75 for off-Broadway shows; Ticketmaster service charges average \$5 to \$7 per ticket, plus an additional \$2 charge per order).

<sup>23</sup> Charges for use of an automated teller machine can be as high as \$3.00 per transaction. See "ATM Fees Earn Chicago 2nd City Label," *Chicago Tribune* (Chicago Sports Final Edition), Aug. 4, 2000, p. 1 (median ATM charge in Chicago and Washington, D.C. areas is \$3; median charge nationally is \$2.25). Thus, for a \$20 withdrawal, the customer could pay a fee amounting to 15 percent of the amount received.

<sup>24</sup> As noted in Galileo's earlier comments, any attempt to regulate the level of booking fees would raise many difficult issues, including how costs should be allocated between participants and subscribers. The cost allocation issue has become even more complicated as CRSs have entered other lines of business. In view of the pace of change in the CRS business, if the Department were to attempt to regulate CRS fee levels, it would have to commit itself to a process of continuing oversight.

they are in the business of processing transactions. A CRS invests huge amounts in developing the capability to process thousands of transactions per second. Every transaction processed, whether an active booking, a passive booking, or a cancellation, uses CRS resources. Thus, it is entirely reasonable for a system to impose a charge in connection with each of these transactions.<sup>25</sup> And in many cases voluntary choices of carriers are responsible for the high level of allegedly “unproductive” transactions processed through CRSs. For example, frequent fare sales and schedule changes initiated by carriers can lead to large volumes of cancellations and rebookings.

Moreover, carriers and their customers in fact derive value from many types of transactions that do not result in actual travel. For example, when a cancellation is processed by a CRS, the carrier does not receive ticket revenue, but that is one less telephone call that airline reservations personnel must handle. Even more important, transmission of the cancellation message releases valuable inventory, allowing the airline to resell the seat. There is no reason to bar CRSs from charging carriers for the processing of this or any other transaction.

#### **E. Subscriber Contract Provisions**

The current CRS rules restrict in various respects the terms and conditions of contracts between CRSs and their subscribers. For example, CRS vendors must offer a three-year subscriber contract option, and contract terms may

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<sup>25</sup> Suggestions that CRSs should charge only for transactions that result in actual travel are similar to an argument that the telephone company should charge for use of its lines only if the deal the parties are negotiating on the telephone goes through. Any such argument would be plainly frivolous.

not exceed five years. 14 C.F.R. § 255.8(a). In addition, minimum use provisions may not be included in subscriber contracts. *Id.* § 255.8(b).

Several commenters argue that the Department should impose even greater restrictions on the terms of subscriber contracts. Interestingly, it is not travel agents that are most vocal on this point. Rather, it is Orbitz, the entity criticized by some travel agents as the vehicle by which carriers will seek to bypass travel agencies.

According to Orbitz, CRSs have monopoly power with respect to travel agents and are able to lock them into restrictive contracts for long periods of time.<sup>26</sup> But the reality is that travel agents are the ones with leverage in this relationship. Competition among CRS vendors to obtain and keep subscribers is fierce. As a result, many subscribers, particularly the larger travel agencies, are able to demand very large financial incentives from CRSs. Many agencies receive substantial up-front payments or loans from their CRS vendors.

Moreover, although most subscribers sign five-year contracts (preferred by subscribers because contracts with longer terms ordinarily have better financial terms than contracts with shorter terms), Galileo's experience is that more and more three-year contracts are now being signed. This has occurred increasingly in the context of consolidation in the travel agency market; as large agencies absorb smaller agencies, the large agencies take the occasion to renegotiate subscriber contracts, demanding additional incentives and, in some cases, shorter contract terms.

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<sup>26</sup> See Orbitz Comments, at 12-14.

Even apart from the consolidation context, many agencies seek more favorable terms just two or three years into a contract. CRSs often must renegotiate contract terms long before a contract expires because the subscriber has been approached by another vendor seeking to convert the subscriber's business. The result is often a better deal for the subscriber. If a CRS concludes that it cannot afford the terms a subscriber is demanding, it is likely to lose the business, since competing vendors are usually willing to buy out the subscriber's existing contract.

In this competitive environment, there is no reason to require shorter contract terms. Because CRSs must offer large financial concessions to obtain and keep subscribers, they need to obtain contractual commitments for a substantial length of time in order to recover their investments. Experience demonstrates that five-year contract terms will not prevent subscribers from switching CRSs or obtaining more favorable terms from the incumbent CRS.

The arguments of Orbitz and Delta that the Department should prohibit CRSs from recovering certain forms of damages when a subscriber breaches its contract<sup>27</sup> should also be rejected. In view of the large capital costs involved in providing hardware for subscriber premises, the substantial up-front financial incentives CRS vendors must offer to obtain subscribers, and the losses in booking fee revenue a CRS faces when a subscriber terminates prematurely, there are clear business reasons for a CRS vendor to seek compensation for its loss. If a vendor should attempt to assess liquidated damages that are not a reasonable approximation of its likely loss from a contract breach, a court will decline to enforce the provision

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<sup>27</sup> Orbitz Comments at 78; Delta Suppl. Comments at 8.

on the ground that it constitutes a penalty.<sup>28</sup> There is no need for the Department to take action on this subject.

Orbitz urges the Department to prohibit productivity pricing.<sup>29</sup> But there is nothing inappropriate about such pricing; volume discounts are a standard business practice. Travel agents strongly opposed a prohibition on productivity pricing when the CRS rules were revised in 1992, and the Department ultimately determined that it should not impose such a prohibition. The Department properly concluded then that productivity pricing can promote efficient use of CRS equipment.<sup>30</sup> There is no basis for a different conclusion today.

Delta's argument that the Department should require CRSs to permit the use of third-party software with terminals they own (Delta Suppl. Comments at 8) should be rejected. The Department recognized in 1992 that CRSs have an interest in controlling use of their own hardware.<sup>31</sup> In any event, Galileo permits subscribers to use a wide range of third-party software with its equipment. Subscribers that want greater latitude are free to obtain third-party hardware.

Galileo has recently deployed a new advanced application interface, XML Select, that will make it more convenient for agencies to use third-party hardware. This new interface provides an open platform, delivering structured data in a

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<sup>28</sup> See *United Air Lines, Inc. v. Austin Travel Corp.*, 681 F. Supp. 176, 186-89 (S.D.N.Y. 1988), *aff'd*, 867 F.2d 737 (2d Cir. 1989) (finding that the liquidated damages provision of an Apollo® contract did not constitute a penalty).

<sup>29</sup> Orbitz Comments at 77.

<sup>30</sup> See 57 Fed. Reg. 43827 (1992).

<sup>31</sup> See *id.* at 43800.

messaging format using standard communications interfaces. XML Select allows a travel agency to build its own interface between third-party equipment and the Apollo® system, minimizing issues of compatibility.

Finally, several airline commenters suggest that CRS vendors should be required to monitor their subscribers to detect abuses of various sorts. For example, Lufthansa wants CRS vendors to ensure that subscribers use neutral displays.<sup>32</sup> Such suggestions should be rejected. CRSs are not in a position to monitor the conduct of thousands of subscribers and to enforce hundreds of airline policies. If the Department concludes that regulation of subscriber displays or other subscriber conduct is in the public interest, the Department should impose such regulation directly on subscribers.<sup>33</sup>

## **II. AIR TRAVEL DISTRIBUTION OVER THE INTERNET**

### **A. Whether to Regulate**

The initial comments display little agreement about whether and to what extent the Department's CRS rules should apply to the Internet. The Internet is still new and is evolving quickly in unpredictable ways, and it has given consumers expanded choices. The Department should be wary of unintended consequences that might flow from regulation of the Internet, and should refrain from precipitous action

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<sup>32</sup> See Lufthansa Comments at 3.

<sup>33</sup> Galileo addressed arguments that CRSs should control alleged "abusive bookings" by subscribers at length in its earlier comments in this proceeding. See, e.g., Comments of Galileo International, L.L.C. in Response to Advance Notice of Proposed Rulemaking, filed Dec. 11, 1997, at 34-40.

that might dampen emerging benefits before they are fully realized. Certainly no comments have made a compelling case to extend CRS regulation to the Internet.

A few comments allege that unwary consumers may be misled by the way some Internet travel providers present information, or that consumers cannot be trusted to understand the complexities of travel options. But the commenters fail to provide any compelling evidence that consumers are in fact misled or harmed. Travelers know their own preferences, and can recognize whether they are getting the information they want. Moreover, Internet users can switch to other providers (including comparison shopping between online services and off-line travel agents) if they are not satisfied with the results they get.

Some commenters argue that the Department should extend its CRS rules to the Internet merely because the European Union has taken a similar step. But a desire to harmonize regulatory regimes by itself is not enough to justify new regulation. While comprehensive regulation is often the "default" mode in Europe, the United States generally takes a more focused regulatory approach that targets particular harms. The Department has required a clear and compelling case that stands on its own, a showing that regulation is needed to avoid a substantial reduction in airline competition, or to protect consumers from deception. The public benefits must be shown to substantially outweigh the costs imposed by the regulation. See page 3 note 2 above. The fact that the European Union, working from a different legal tradition in which regulation is far more pervasive, has adopted regulations cannot substitute for that justification.

## **B. The Importance of Even-Handed Regulation**

While Galileo does not support regulation of Internet services, it objects most strenuously to regulation that would place unequal burdens on Galileo as compared to its Internet competitors. Galileo emphasized in its initial comments that the Department's guiding principle must be to regulate evenhandedly, so that competitors have an equal opportunity to compete in this dynamic field. But some instead urge the Department to impose regulations on one category of competitors but not others. Thus, for instance, Expedia (which has no airline owners) argues that Internet services that have a minimum level of airline ownership should be subject to all CRS regulations, but that competitors offering the same services that have no airline owners should remain free from regulation. Such an approach would impose unequal costs and burdens on Galileo's Internet services.

Such self-serving positions should be rejected. Hobbling one group of service providers is likely to distort the competitive process and retard innovation. If the Department concludes that regulation of the Internet is appropriate, it should impose those requirements equally on all companies that offer the same services.

## **C. Restrictions on Carrier Choices About Fare Availability**

A number of comments focus specifically on the new Internet collaborations, Orbitz and Hotwire, formed by the major airlines to distribute tickets to consumers over the Internet, expressing concerns that these new ventures may produce significant anticompetitive effects in markets for air transportation and ticket distribution services.



The five major airline owners of Orbitz account for over 80 percent of domestic air transportation. Those carriers, through the Orbitz venture, have apparently reached "Charter Associate Agreements" with at least two dozen additional airline partners. In its September 22 comments (at 17-18), Galileo noted concerns that the Orbitz participants may restrict information, fares, or participation in other systems and services in order to favor Orbitz. Others agree: There is widespread concern that the participating airlines will act together through the Orbitz and Hotwire ventures in a way that will effectively make the lowest discount air fares available on only one or the other of those two services.

The initial comments reveal specific details of the Orbitz structure and agreements that heighten Galileo's concerns: It appears that the airlines collaborating through the Orbitz venture have agreed to terms that effectively give Orbitz exclusive access to the lowest air fares.

Orbitz contends that the airlines participating in Orbitz will have economic incentives to offer low fares to as many distribution outlets as possible, not just Orbitz. That claim is disingenuous at best, since it ignores the opposite and powerful economic incentives created by the Orbitz structure and agreements.<sup>34</sup> The Orbitz Charter Associate Agreements impose obligations on all the participating airlines (not just owners) to provide significant financial and other support to the Orbitz collaboration. For example, each airline must provide promotional, advertising

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<sup>34</sup> As other comments have pointed out, that claim is also contradicted by carrier announcements that Orbitz will have exclusive access to the lowest fares on the Internet. *E.g.*, Interactive Travel Services Association Comments at 2; Sabre Comments at 11 n. 3.

and marketing support worth many millions of dollars each year.<sup>35</sup> Each Charter Associate also agrees to provide Orbitz all its published fares, including all promotional fares or other discounted fares available on the airline's own website or elsewhere, "on a MFN basis," that is, on "terms . . . equal to or better than the most favorable terms and conditions offered . . . to any other Internet Travel Provider Site."<sup>36</sup> The Agreement recites that it is "non-exclusive." But as the American Antitrust Institute points out, the MFN obligations are intertwined with the clauses imposing financial and marketing obligations: An Associate airline can avoid a substantial portion of its marketing and promotional obligations by making promotions or fares available exclusively to Orbitz, and withholding them from other Internet Travel Sites.<sup>37</sup>

The result of the provisions of the Charter Associate Agreements is that airlines will have significant incentives to withhold promotional and discount fares from any competing CRS or third-party Internet provider and make them available only through Orbitz or the airline's own Website. Moreover, as a result of their substantial investment to launch Orbitz, the owner airlines will likewise have strong incentives to withhold fares and other features from competing CRS and Internet services. Thus, the likely result of the Orbitz collaboration among airlines will be to restrain significantly the competition among travel distribution services.

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<sup>35</sup> Airline Charter Associate Agreement § 2.2 & Exhibit B. A copy of this agreement is provided as Exhibit 4 to the Travelocity Comments.

<sup>36</sup> Airline Charter Associate Agreement § 2.1(b) & Exhibit A.

<sup>37</sup> See American Antitrust Institute Comments at 6-7.

Orbitz argues that consumers can go to a different Internet provider if it offers better features or services than Orbitz. But that ignores the distorting effect that the Orbitz agreements among carriers will have: Consumers will turn away from other Internet travel providers that cannot give them access to the lowest available fares, even if those services offer better functionality, more convenient interfaces, or other benefits that Orbitz does not match.

While the Department should take appropriate action to prevent the Orbitz collaboration from having these harmful effects, it should proceed cautiously, taking care that it does not impose unnecessary regulation on the new Internet channel. The Department should bear in mind that exclusive arrangements and MFN clauses may have procompetitive features when they do not involve multiple airline agreements.<sup>38</sup> The Department therefore should reject suggestions that it adopt expansive rules that prohibit all such arrangements. Instead, it should take a cautious and measured approach by prohibiting groups of airlines from agreeing among themselves, through MFN provisions or otherwise, to make published fares available exclusively through airline-controlled ventures. Each individual airline should be free, however, to act unilaterally to offer fares exclusively on its own website, or to enter into exclusive fare arrangements or MFN commitments with third-party services that do not involve agreements among multiple airlines.

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<sup>38</sup> Exclusive deals for promotional prices may make carrier entry into a particular market easier, because it will take other carriers longer to detect the lower prices, allowing the entrant to gain a foothold before the other carriers reduce their prices. Or they may foster uncertainty about current prices, forestalling oligopoly pricing effects or coordinated pricing.

#### **D. The "Opt-Out" Argument**

A few airlines argue that the Department should allow them to "opt out" of CRS service in connection with sales made over the Internet, suggesting that a CRS's provision of service that includes transactions by both traditional "bricks and mortar" travel agent subscribers and Internet-based subscribers somehow amounts to improper "tying." These contentions are based on a flawed premise. The CRS service that Galileo provides to airlines comprises a single service that cannot sensibly be divided into "separate and distinct commodities" (Delta Comments at 31) on the basis of different subscribers, different geographic regions, or some other arbitrary grouping.

Galileo operates a single, undifferentiated service that processes bookings from many sources, offering the same capabilities to airlines however the CRS database is accessed. The subscribers are overwhelmingly travel agents and corporate travel departments. Some of these travel agent subscribers are venturing onto the Internet, and some of those Internet ventures include consumer booking features that use Galileo's CRS as the booking engine. Galileo also provides the booking engine for a few Internet-based subscribers, as well as for ual.com and TRIP.com. But the important point is that the service provided to the airline is the same, no matter who the subscriber may be, where it is located, or whether Galileo's own dedicated communications network or the Internet was used in connection with the transaction. Galileo transmits fare and schedule information from the airline to subscribers, and processes and transmits sales and booking transactions for the airline.

To shore up its claims of “separate and distinct commodities,” Delta strains to draw a distinction between Sabre’s “dedicated network linked to professional travel agents” on the one hand and the “Internet services provided to individual travelers” by Sabre’s Travelocity on the other hand. But this depiction does not purport to describe Galileo’s services to Delta and other airlines; it is limited to the operations of Sabre and its affiliate Travelocity. Thus, it ignores the fact that most of Galileo’s CRS bookings that involve the Internet are made through travel agents and other subscribers that are not affiliated with Galileo. Galileo provides airlines the same CRS services for bookings from these Internet-based subscribers as it does for bookings from more traditional subscribers; indeed, many subscribers with bookings from Internet sites are also traditional “bricks and mortar” travel agents.

Moreover, such claims ignore the substantial changes that are eroding whatever differences Delta seeks to identify. Travel agents are establishing a virtual presence on the Internet to complement their physical “bricks and mortar” operations, and their customers will increasingly use both the Internet and more traditional telephone calls or visits to make bookings through those agents. Predictions in this fast-changing business are uncertain, but it may be that virtual, on-line travel services will eventually provide telephone service or enter into alliances with traditional travel agents, to complement their Internet presence. Such convergence to “clicks and mortar” business models, combining traditional modes of service with Internet function and accessibility, may become common.<sup>39</sup>

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<sup>39</sup> See, e.g., Bear Stearns, “Internet Travel: Point, Click, Trip” (Document OST 1997-2881-130) at 35.

For all these reasons, there is no basis for Delta's claim that CRS services amount to a "classic tying arrangement" involving two separate products that is prohibited by the Sherman Act. Airlines receive the same kinds of data processing and transmission services for their transactions with agents and customers regardless of the media or channel used. Delta cites no case (and Galileo is not aware of any) in which a court has found the necessary separate products in those circumstances.<sup>40</sup>

Nor is there any other basis for the Department to require CRSs to allow airlines to opt out of services provided to certain users, or to require that Galileo unbundle its CRS services to suit every individual airline preference. There is no showing that the ability of subscribers and consumers to use the Internet to make CRS bookings has had any negative effect on airline competition. And there is no claim that consumers are receiving inaccurate or misleading information as a result of the use of CRSs as booking engines for Internet services. Furthermore, the claim that carriers fear "abusive" bookings by consumers rings hollow in view of the fact that most carriers are now selling transportation through their own websites and other Internet channels.<sup>41</sup>

Far from remedying any harm to competition or consumer welfare, the primary effect of the proposed "opt out" rule would be to impede competition.

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<sup>40</sup> Another prerequisite for a tying claim is a showing that the seller has substantial market power in the tying product. As discussed at pages 4-6 above, Galileo does not believe that such a showing can be made.

<sup>41</sup> The Department should not lose sight of the fact that bookings made using the Internet are still a very small portion of total airline bookings, and, while they are expected to grow rapidly, they are likely to remain a small portion of total bookings for some time to come. See, e.g., Bear Sterns, "Internet Travel: Point, Click, Trip" (Document OST 1997-2881-130) at 9, 47.

Travel agents and other subscribers have just begun to venture onto the Internet with booking sites and other services. These new Internet-based methods of distribution for air travel have brought substantial benefits to consumers and to competition, even at this early stage. If travel agents and others cannot rely on CRSs as comprehensive booking engines, they are unlikely to develop robust competitive Internet alternatives in the near term. Even the more established Internet travel services would be much less effective competitors if an “opt out” rule were in place.<sup>42</sup>

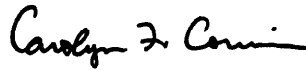
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<sup>42</sup> It is notable that these effects of the proposed rule would advantage Orbitz, the airlines’ own venture, and the airlines’ individual websites. It is little wonder, then, that some airlines advocate such a rule. But the Department should not entertain proposals that risk reducing competition in this way.

## CONCLUSION

For both CRS services and Internet services, the Department should either eliminate or tailor its regulation in a manner that provides all participants with an equal opportunity to compete. Proposals that are inconsistent with the principle of even-handed regulation should be rejected.

Respectfully submitted,



CAROLYN F. CORWIN  
DAVID W. ADDIS  
RAYMOND A. ATKINS  
Covington & Burling  
1201 Pennsylvania Avenue, N.W.  
Washington, D.C. 20004-2401  
202-662-6000

Counsel for  
Galileo International, L.L.C.

ANTHONY C. SWANAGAN  
Senior Vice President and  
General Counsel  
CATHY L. CUPP  
Senior Counsel and Legal Director -  
International  
THOMAS J. DEMAY  
Regulatory Affairs Counsel

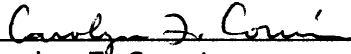
Galileo International, L.L.C.  
9700 West Higgins Road  
Rosemont, Illinois 60018  
847-518-4800

October 23, 2000



### CERTIFICATE OF SERVICE

I hereby certify that on this 23rd day of October, 2000, I caused copies of the foregoing Reply Comments of Galileo International, L.L.C. to be sent by first class mail, postage prepaid, to those named on the attached Service List.

  
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Carolyn F. Corwin

SERVICE LIST - DOCKET OST 97-2881 -  
October 23, 2000

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Marshall S. Sinick  
James V. Dick  
Squire, Sanders & Dempsey, L.L.P.  
1201 Pennsylvania Avenue, N.W.  
Washington, D.C. 20004

David H. Coburn  
Carol R. Gosain  
Steptoe & Johnson L.L.P.  
1330 Connecticut Avenue, N.W.  
Washington, D.C. 20036

Joanne W. Young  
David M. Kirstein  
Alan F. Enslin  
Baker & Hostetler, L.L.P.  
Washington Square, Suite 1100  
1050 Connecticut Avenue, N.W.  
Washington, D.C. 20036

Paul M. Ruden  
Senior Vice President  
American Society of Travel  
Agents, Inc.  
1101 King Street  
Alexandria, Virginia 22314

Jon F. Ash  
Charles R. Chambers  
Global Aviation Associates, Ltd.  
1800 K Street, N.W.  
Suite 1104  
Washington, D.C. 20006

Don H. Hainbach  
Boros & Garofalo, P.C.  
1201 Connecticut Avenue, N.W.  
Washington, D.C. 20036

R. Bruce Keiner, Jr.  
Lorraine B. Halloway  
Crowell & Moring L.L.P.  
1001 Pennsylvania Avenue, N.W.  
Washington, D.C. 20004-2595

Arthur J. Molins  
General Counsel North America  
Deutsche Lufthansa Aktiengesellschaft  
1640 Hempstead Turnpike  
East Meadow, New York 11554

Megan Rae Rosia  
Managing Director, Government Affairs  
& Associate General Counsel  
Northwest Airlines, Inc.  
901 - 15th Street, N.W.  
Suite 310  
Washington, D.C. 20005

Glenn Fuller  
Associate General Counsel  
Northwest Airlines, Inc.  
5101 Northwest Drive  
Department A1180  
St. Paul, MN 55111

David A. Schwarte  
Executive Vice-President & General Counsel  
Sterling L. Miller  
Senior Managing Attorney  
Sabre Inc.  
4255 Amon Carter Boulevard  
MD 4204  
Fort Worth, TX 76155

Donald L. Pevsner  
Attorney-at-Law  
1765 East Riviera Drive  
Merritt Island, Florida 32952

Edward P. Faberman  
Michelle M. Faust  
Air Carrier Association of America  
1500 K Street, N.W.  
Suite 250  
Washington, D.C. 20005-1714

Robert E. Cohn  
Alexander Van der Bellen  
Shaw Pittman  
2300 N Street, N.W.  
Washington, D.C. 20037

Mark Silbergeld  
Co-Director - Washington Office  
Janell Mayo Duncan  
Legislative Counsel - Washington Office  
Consumers Union  
1666 Connecticut Avenue  
Suite 310  
Washington, D.C. 20009-1039

Carl B. Nelson, Jr.  
Associate General Counsel  
American Airlines, Inc.  
1101 - 17th Street, N.W.  
Suite 600  
Washington, D.C. 20036

R. Bruce Wark  
Senior Attorney  
American Airlines, Inc.  
4333 Amon Carter Boulevard  
MD5675  
DFW Airport, TX 75261

Robert P. Silverberg  
Silverberg, Goldman & Bikoff  
1101 - 30th Street, N.W.  
Suite 120  
Washington, D.C. 20007

Charles D. Simpson  
Craig M. Cibak  
Zuckert, Scoult & Rasenberger  
888 - 17th Street, N.W.  
Suite 600  
Washington, D.C. 20006-3309

Frank J. Costello  
Jol A. Silversmith  
Paul E. Schoellhamer  
Zuckert, Scoult & Rasenberger  
888 - 17th Street, N.W.  
Suite 600  
Washington, D.C. 20006-3309

Jose G. da Rosa  
Chairman & CEO  
Balboa Travel Management  
5414 Oberlin Drive  
San Diego, CA 92121-4745

Marshall A. Fein  
Attorney at Law  
1323 Hallmark  
San Antonio, Texas 78216

Albert A. Foer  
President  
The American Antitrust Institute  
2919 Ellicott Street, N.W.  
Washington, D.C. 20008

Don Rounds  
President  
The Consumer Alliance  
115 SW. Allegan  
Suite 500  
Lansing, MI 48933

Donald A. Kaplan  
Brian McCalmon  
Preston Gates Ellis & Rouvelas Meeds LLP  
1735 New York Avenue, N.W.  
Washington, D.C. 20006

Marianne McNerney  
National Business Travel Association  
1650 King Street, Suite 401  
Alexandria, VA 22314

Andrew B. Steinberg  
Executive Vice President Administration,  
General Counsel, and Corporate Secretary  
Keenan M. Conder  
Associate General Counsel  
Travelocity.com  
15100 Trinity Boulevard  
Fort Worth, TX 76155

Bruce H. Rabinovitz  
Jeffrey A. Manley  
Wilmer, Cutler & Pickering  
2445 M Street, N.W.  
Washington, D.C. 20037-1420

Bruce Bishins, CTC  
President and CEO  
United States Travel Agent Registry  
511 Avenue of the Americas  
New York, NY 10011-8436

Edward P. Faberman  
Michelle M. Faust  
Ungaretti & Harris  
1500 K Street, N.W. - Suite 250  
Washington, D.C. 20005-1714

Hal F. Rosenbluth  
Chairman and Chief Executive Officer  
Rosenbluth Travel  
2401 Walnut Street  
Philadelphia, PA 19103

Thomas Ray (*by messenger*)  
Office of the General Counsel  
U. S. Department of Transportation  
400 Seventh Street, S.W.  
Room 4102  
Washington, D.C. 20590